REDACTED VERSION

STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2004-553

October 29, 2004

NORTHERN UTILITIES, INC.,
Proposed Cost of Gas Factor
for November 2004 – April 2005

ORDER

Welch, Chairman; Diamond and Reishus, Commissioners

I. SUMMARY

We approve Northern Utilities, Inc.'s (Northern) Cost of Gas Factor (CGF) for the 2004 – 2005 Winter Period as proposed in the October 13, 2004 update, and direct Northern to find ways to mitigate its excess gas supply commitments. We also approve an Environmental Response Cost Adjustment (ERCA) of $0.0095 per Ccf.

II. PROCEDURAL HISTORY

On August 16, 2004, pursuant to 35-A M.R.S.A. § 4703 and Chapter 430(2) of the Commission's Rules, Northern filed its proposed CGF for the Winter 2004 – 2005 gas usage period. Northern also proposed a change in the ERCA rate in accordance with the settlement approved in Docket No. 96-678. On August 24, 2004, Northern made a revised filing that corrected reconciliation amounts for last winter's gas costs. The Commission issued a Notice of Proceeding to intervenors in prior CGF cases and by publication in newspapers of general circulation in Northern's service area, noting that the Company's proposed rates, if approved, would increase the average residential customer's total bill by 3.57% over last winter period.

The Office of the Public Advocate (OPA) intervened. To investigate the proposed CGF changes, the Advisory Staff issued data requests to the Company on its filing. A preliminary hearing was held on September 22, 2004, at which the Advisory Staff and the parties explored the issues raised by this filing. An additional conference was held on October 4, 2004 to further discuss issues related to the Company's gas supply needs and contracts. The Company provided responses to Oral Data Requests made at both conferences. At the October 4th conference, Northern indicated that it would make a revised CGF filing to incorporate an updated forecast of Winter Period commodity costs prior to the implementation of rates if, in its view, changes in NYMEX gas price futures warranted. On October 13, 2004, Northern filed a revised proposed CGF rates using recent NYMEX futures.

III. RECORD

The record in this proceeding includes all filings, data responses, transcripts, and any other materials provided in the proceeding.

IV. DISCUSSION

A. Overview of Proposed Rates

In its October 13, 2004 update, Northern proposed the following 2004 Winter Period CGF rates on a per hundred cubic feet (Ccf) basis to become effective November 1, 2004:

Class	Rate	% Average Bill Change from Winter 2003 – 2004
Residential - Heat (R-2)	$1.1508	6.6
Residential – Non-Heat (R-1)	1.1504	6.6
Small Commercial - Low Winter Use (G-50)	1.0407	10.1
Small Commercial - High Winter Use (G-40)	1.1635	4.1
Medium Commercial - Low Winter Use (G-51)	1.0346	11.3
Medium Commercial - High Winter Use (G-41)	1.1622	5.1
Large Commercial/Industrial – Low Winter Use (G-52)	1.0560	28.2
Large Commercial/Industrial – High Winter Use (G-42)	1.1388	7.5

The proposed ERC rate of $0.0095 per Ccf is calculated to allow for recovery of the portion environmental clean-up costs incurred by Northern during the period July 2003 through June 2004, in accordance with the settlement in Docket No. 96-678.

B. Issues

1. 2003 – 2004 Winter Period Under-Collection

Maine law allows for the recovery of prior period cost of gas under-collections, with interest, during the next corresponding seasonal period. 35-A M.R.S.A. § 4703 and Chapter 430 of the MPUC Rules. In its filing, Northern reported an under-collection of approximately $299,359 from the 2003 – 2004 Winter Period.[1] Staff has reviewed Northern's figures and finds them to be consistent with the usual methodology. The 2003 – 2004 Winter Period under-collection increases the proposed 2004-2005 Winter Period cost of gas by approximately $0.0101 cents per ccf for all customer classes.

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[1] This comprises an over-collection of $281,951 in demand costs and an under-collection of $581,310 in commodity costs.

We note that the effects on the proposed CGF on the G-52 class will result in a significant increase in average bills over last year compared to other rate classes. While this is of some concern, the G-52 rate itself is consistent with the rates for other low winter use customers and the allocation of gas costs (including reversed credit amounts) to this class is equitable. Given the gas price outlook, we anticipate similar issues could arise if we deferred a portion of this increase until next winter period. Accordingly, we approve recovery of these amounts in the upcoming winter period.

2. <u>ERCA Adjustment</u>

As allowed in Docket No. 96-786, Northern has adjusted its ERCA rate for the Winter period to include the amortization of the costs incurred during the period July 2003 through June 2004 for environmental clean up of its Manufactured Gas Plant sites to reflect the recoveries during the Winter 2003 – 2004 period. We have reviewed Northern's calculations, and the supporting invoices, and find them in compliance with our Order in Docket No. 96-786 and approve the ERCA rate as filed on August 16, 2004.

3. <u>Hedging</u>

Northern has included costs related to its hedging plan. Northern calculated the estimated profit or loss based upon the most recent NYMEX futures prices for the hedges that it has purchased for the upcoming winter period supply. Actual profits or losses for the 2004 - 2005 Winter Period will be reconciled when Northern files its 2005 - 2006 Winter Cost of Gas filing.

Northern included the costs, along with the profits or losses, of the 2004-2005 winter period supply hedges to all sales customers in its proposed rates for the upcoming winter period. This is reasonable and consistent with the intent of the approved hedging plan.

4. <u>Gas Supply Review</u>

During our examination of Northern's cost of gas filing, we examined one of the contracts that Northern currently has to obtain gas supply that it needs to provide sales service to its customers. Our initial review indicates that some of its contracted supplies are in excess of Northern's current needs. We understand that Northern entered into several long-term contracts when Northern's projected customer loads were significantly greater. Subsequently, many changes have taken place both in Northern's corporate organization and the gas market that may have contributed to Northern's greatly diminished gas sales growth in Maine. Northern now indicates that if it could unilaterally change the quantities in its most recently entered peaking supply contract with Duke Energy Trading and Marketing, one of the alternative supplies entered into at the time of the termination of the Wells project, it would purchase substantially less in the remaining years of the contract, as shown in Confidential Appendix A.

The mere fact that Northern would, with perfect hindsight, modify the amounts it purchased does not, in itself, imply any error on Northern's part. However, it does suggest we should focus some attention on how well Northern's current supply portfolio matches its customer demand to determine whether its gas costs are reasonable and its gas supply contracting and management decisions have been prudent.

In the face of a potential surplus, Northern would presumably look to sell its excess either through increased retail sales service (perhaps by increasing the number of its sales customers or the usage per customer) or on the wholesale market. However, information provided in this case indicates that, after merging with NiSource, marketing resources and positions serving Maine were drastically cut. In 2000 and 2001, Northern's Marketing and Sales budget was $600,000 to $700,000. This declined to $250,000 in 2002 and $150,000 to $175,000 in 2003 and 2004. Northern states that the Company recently decided to add back marketing positions serving Maine in an effort to avoid further attrition of its customer load and to achieve a growth level of approximately 1%. More investigation will be necessary to determine to what extent the elimination of marketing resources, rather than factors such as rising gas prices or the migration of sales customers to transportation-only service, is responsible for the significant decrease in Northern's current load as compared to loads that were projected in 1999.[2] When gas supply commitments have been rendered excessive as a result of management decisions, the question arises as to whether disallowance of such excess costs in rates may be warranted, to the extent they result from imprudent management acts.

We cannot know today to what extent Northern will, in fact, have surplus supplies under its existing supply contracts in future cost of gas periods. This will depend on its success in mitigating the excess through increased retail sales, including the effect of any marketing campaigns, as well as any efforts Northern makes to sell its excess to others at the wholesale level. We intend to monitor this over the upcoming year.

To further evaluate Northern's gas supply commitments, we direct Northern to file in its next cost of gas filing, a detailed summary of its existing contracts for both commodity and demand, including the term and pricing provisions of the contract. In addition, Northern should provide the demand forecast and growth assumptions upon which it relied when it contracted for alternative supplies to take the place of the terminated Wells project, as well as its current demand forecast.

In the meantime, we expect Northern to pursue mitigation of the cost of its excess gas supply commitments, whether by capacity release, reformation of the agreements, or other means, and to tailor its gas supply portfolio to current, reasonable

[2] In its exceptions, Northern suggests that the Commission has failed to act on Northern's request that it be determined to be the provider of last resort for transportation-only customers, however, there is no such request pending. Northern is free to file such a request with us for consideration at any time.

projections of its customer demand. Northern should also report on the results of these efforts in its next cost of gas filing.

V. CONCLUSION

Based upon our review, we determine that the Cost of Gas Factor proposed by Northern reflects its estimated cost to provide gas service to its customers during the 2004 – 2005 Winter Period. We will further investigate Northern's gas supply portfolio and factors such as the extent to which management decisions may have contributed to excess supply, as well as Northern's efforts to mitigate its anticipated excess supply and its costs, to determine whether all existing gas supply costs are reasonable and should be included in rates.

Accordingly, we

O R D E R

1. That Northern Utilities, Inc.'s Forty-fifth Revised Sheet No. 20.1 constituting its Cost of Gas Factor for the period November 1, 2004, through April 30, 2005, filed on October 13, 2003, is approved for gas consumed on or after November 1, 2004;

2. That Northern Utilities, Inc.'s Fifteenth Revised Sheet No. 34.3, the Environmental Response Cost Adjustment rate schedule filed on August 16, 2004, is approved and will become effective November 1, 2004; and

3. That Northern Utilities, Inc., in its next Cost of Gas Factor filing, shall file information on its contracts to meet is gas supply needs as discussed in the body of this order.

Dated at Augusta, Maine, this 29th day of October, 2004.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Diamond
Reishus

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within **21 days** of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.